Supreme Court, U. S.
FILED
SEP 29 1977
MICHAEL RODAK, JR., CLERK

No. 77-331

In the Supreme Court of the United States

OCTOBER TERM, 1977

ELMER E. MILLS,

Petitioner,

vs.

THE ELECTRIC AUTO-LITE COMPANY, MERGENTHALER LINOTYPE COMPANY and AMERICAN MANUFACTURING COMPANY,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

JEROLD S. SOLOVY
JOAN M. HALL
Attorneys for Respondents
One IBM Plaza
Chicago, Illinois 60611

JENNER & BLOCK
MICHAEL J. ROVELL
ROBERT L. GRAHAM
JAYNE W. BARNARD
EUGENE R. WEDOFF
Of Counsel

UNITED STATES LAW PRINTING CO., CHICAGO, ILLINOIS 60618 (312) 525-6561

TABLE OF CONTENTS

	PAGE
Questions Presented	1
The Mandate Of This Court	2
Additional Statement Of The Case	4
The Merger Partners	4
Auto-Lite	4
Mergenthaler	5
The Merger Terms	5
The Trial	7
The Decision Of The District Court	8
The Unanimous Decision Of The Court Of Appeals	8
Reasons For Denying The Writ	10
I. The Mandate Of This Court Has Been Fulfilled	10
A. The Lower Courts' Rejection Of Petitioner's Post-Merger Damage Theory Requires No Further Review	10
(1) Commingling Precluded The Application Of Petitioner's Post-Merger Damage Theory	10
(2) Petitioner's Post-Merger Damage Theory Was Not Sustained By The Evidence	11

PAGE

(3) Petitioner's Post-Merger Damage Theory Failed As A Matter Of Law 12

B. The Factual Determination That The Merger Terms Were Fair Raises No Question Worthy Of Consideration By This Court 15

(1) The Weight Of The Evidence Demonstrated The Fairness Of The Merger Terms 15

(2) The Court Of Appeals Properly Determined That The Merger Terms Were Fair 16

C. Denial Of Additional Attorneys' Fees By The Court Of Appeals Does Not Merit Review By This Court 21

II. This Case Is Inappropriate For This Court's Review Because The Legal Standard Of Materiality In *TSC* v. *Northway* Was Never Applied Below 24

III. The Refusal To Award Damages In The Absence Of Monetary Injury Is In Accord With Established Law 26

Conclusion 28

TABLE OF CASES

PAGE

Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972) 14

Alyeska Pipeline Service Co. v. Wilderness Society, 421 U.S. 240 (1975) 22

Bangor Punta Operations, Inc. v. Bangor & Aroostook Railroad, 417 U.S. 703 (1974) 27, 28

Berenyi v. Immigration Director, 385 U.S. 630 (1967) 12

Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) 27

Borg v. International Silver Co., 11 F.2d 147 (2d Cir. 1925) 18

Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477 (1977) 27

David J. Greene & Co. v. Schenley Industries, Inc., 281 A.2d 30 (Del. Ch. 1971) 18, 19

Dasho v. Susquehanna Corp., 461 F.2d 11 (7th Cir.), *cert. denied*, 408 U.S. 925 (1972) 18

E. I. duPont de Nemours & Co. v. Collins, ... U.S. ....., 45 U.S.L.W. 4668 (1977) 18

Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) 23

Gallois v. West End Chemical Co., 185 Cal. App. 2d 765, 8 Cal. Rptr. 596 (1960) 19

General Talking Pictures Corp. v. Western Electric Corp., 304 U.S. 175 (1938) 21

Gerstle v. Gamble-Skogmo, Inc., 478 F.2d 1281 (2d Cir. 1973) 14

Graver Manufacturing Co. v. Linde Co., 336 U.S. 271 (1949) 12

PAGE

In re Talley Industries, Inc., [1969-70 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶77,774 (1970) 18

Janigan v. Taylor, 344 F.2d 781 (1st Cir.), *cert. denied*, 382 U.S. 879 (1965) 14

Levin v. Mississippi River Corp., 59 F.R.D. 353 (S.D. N.Y. 1973) 18

Mills v. Electric Auto-Lite Co., 396 U.S. 375 (1970) 1, 3, 10, 11, 21, 22, 23, 24, 25, 26

Mills v. Electric Auto-Lite Co., 403 F.2d 429 (7th Cir. 1968) 2, 24, 25

Mills v. Electric Auto-Lite Co., 281 F. Supp. 826 (N.D. Ill. 1967) 2

Pepper v. Litton, 308 U.S. 295 (1939) 18

Rondeau v. Mosinee Paper Corp., 422 U.S. 49 (1975)..26, 27

Santa Fe Industries, Inc. v. Green, ... U.S. ....., 45 U.S.L.W. 4317 (1977) 13

Schwabacher v. United States, 334 U.S. 182 (1948) 18

TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976) 3, 24, 25

United States v. American Railway Express Co., 265 U.S. 425 (1924) 25

OTHER AUTHORITIES

Brudney & Chirelstein, *Fair Shares in Corporate Mergers and Takeovers*, 88 Harv. L. Rev. 297 (1974) 20, 21

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-331

ELMER E. MILLS,

Petitioner,

vs.

THE ELECTRIC AUTO-LITE COMPANY, MERGENTHALER LINOTYPE COMPANY and AMERICAN MANUFACTURING COMPANY,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

Respondents pray that the petition for a writ of certiorari be denied.

QUESTIONS PRESENTED

This case, arising from the 1963 merger of The Electric Auto-Lite Company ("Auto-Lite") and Mergenthaler Linotype Company ("Mergenthaler"), presents no issue worthy of review by this Court. The unanimous decision of the United States Court of Appeals for the Seventh Circuit correctly applied the clear mandate of this Court in *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970). The only questions presented by this case are:

(1) Whether this Court should grant certiorari to review evidentiary findings that petitioner suf-

fered no damage and, in fact, substantially benefitted from the merger; and

(2) Whether this Court should grant certiorari to review the finding that although petitioner was entitled to attorneys' fees and expenses for establishing liability, he was not entitled to additional fees and expenses for his unsuccessful attempt to prove damages.

THE MANDATE OF THIS COURT

Prior to the merger of Auto-Lite and Mergenthaler in June 1963, two Auto-Lite minority shareholders filed a class and derivative action.[1] Plaintiffs alleged, *inter alia*, that the merger proxy statement violated Section 14(a) of the Securities Exchange Act of 1934 by placing in boldface type a recommendation of the Auto-Lite board favoring the merger without giving similar emphasis to the control relationship between Mergenthaler and Auto-Lite.

In September 1967, the District Court entered a summary judgment of liability for the alleged proxy deficiency. 281 F. Supp. 826 (N.D. Ill. 1967). In November 1968, the Court of Appeals reversed that judgment on the ground that no causal connection had been demonstrated between the deficiency in the proxy statement and the vote approving the merger. 403 F.2d 429 (7th Cir. 1968).

In January 1970, this Court reversed the Court of Appeals in part and held that where a proxy statement has been found to contain a material defect, causation need

[1] One of the named plaintiffs, Louis Susman, has not joined in the petition for certiorari. Petitioner has failed to inform this Court of this fact or the reason for Susman's withdrawal. See Supreme Court Rule 21(4).

not be shown. 396 U.S. at 384-85.[2] The Court stated that its holding implied "nothing about the form of relief to which [petitioner] may be entitled." 396 U.S. at 386. The Court held that "damages should be recoverable only to the extent that they can be shown." 396 U.S. at 389.

The Court discussed two possible theories under which damages might be proven—"earnings or earnings potential" and "fairness":

> "[1] [W]here, as here, the misleading aspect of the solicitation did not relate to terms of the merger, monetary relief might be afforded to the shareholders only if the merger resulted in a reduction of the earnings or earnings potential of their holdings. . . . [2] If commingling of the assets and operations of the merged companies makes it impossible to establish direct injury from the merger, relief might be predicated on a determination of the fairness of the terms of the merger at the time it was approved." 396 U.S. at 388-89.

The Court noted that this case might never produce a damage award but held that petitioner was entitled to recover reasonable attorneys' fees and expenses for establishing the deficiency in the proxy statement. 396 U.S. at 396. The Court held that such an award, even without the imposition of damages, would serve the purpose of "corporate therapeutics." 396 U.S. at 396. The Court stated that the question of reimbursement for future fees and expenses should be resolved by the lower courts after the issue of relief had been litigated. 396 U.S. at 390 n.13.

The trial and appeal on the issue of relief, following remand from this Court, are the subject matter of the petition.

[2] This Court did not review the question of whether the alleged defect in the proxy statement was material. 396 U.S. at 381 n.4. See discussion of *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438 (1976), at pp. 24-25, *infra*.

ADDITIONAL STATEMENT OF THE CASE

Petitioner's statement of the case is inadequate and omits pertinent facts found by the courts below.

The Merger Partners.

Auto-Lite.

Historically, Auto-Lite engaged primarily in the manufacture of automotive parts and equipment. (App. 30a, 51a.)[3] At the time of the 1963 merger, 78% of Auto-Lite's sales were made to the automotive industry. (PX 1, p. 24.) As the District Court found, Auto-Lite was adversely affected by the decision of General Motors, Ford, and Chrysler to manufacture and distribute their own automotive parts. (App. 31a.) By the time of the merger, this industry development had caused Auto-Lite to lose a substantial volume of business. (App. 31a-33a.)[4]

In 1962, Auto-Lite earned 1.8% on net sales, as compared to the 5.6% industry average of the other major auto parts companies. It also earned the least on book value (3.2% as against 11.3% for the industry). (DX 45.) Based upon the evidence, the District Court found that at the time of the merger Auto-Lite was at a "life cycle crossroad" and faced "serious market risks." (App. 51a.)

---

[3] "Pet." refers to the petition for certiorari; "App." to petitioner's appendix; "PX" and "DX" to petitioner's and respondents' trial exhibits, respectively; "Tr." to the transcript of trial testimony.

[4] For many years, Chrysler had been Auto-Lite's principal customer. As a result of Chrysler's decision to manufacture many of its own parts, Auto-Lite's sales to Chrysler decreased from $134 million in 1957 to $21.6 million by 1962. (App. 30a-31a.)

Mergenthaler.

Prior to the merger, Mergenthaler owned 54% of Auto-Lite. (App. 36a.) Mergenthaler was a world leader in the production and distribution of linotype machines and other typesetting equipment. (App. 34a-35a.) Mergenthaler enjoyed the largest market share in the typesetting industry and had extensive international operations. (App. 35a; PX 1, p. 34; Tr. 2252.) Unlike Auto-Lite, Mergenthaler faced no serious market risks. (App. 51a.)

The District Court found that, as of the merger date, Mergenthaler was protected "from adverse business cycles" (App. 35a) and had "far more stable" profits and sales than Auto-Lite. (App. 51a.) The District Court further found that Mergenthaler provided Auto-Lite with a "stable and certain" merger partner. (App. 23a.)

The Merger Terms.

The merger became effective on June 28, 1963. (App. 24a.) Under the merger terms, the Auto-Lite minority shareholders received 1.88 shares of convertible preferred stock in the successor corporation ("Eltra") for each share of Auto-Lite exchanged. (App. 4a.)[5]

The Auto-Lite shareholders received the following benefits under the merger exchange.

Market Price. During the first quarter of 1963, the average weekly market price of Auto-Lite stock was $52.25. (App. 17a.) The average market price of equivalent Eltra

---

[5] The Eltra preferred shares were convertible into common shares on a one-to-one basis for the first two years following the merger and on a slightly decreasing basis for the next three years. (App. 4a-5a.) The Mergenthaler shareholders received one Eltra common share for each Mergenthaler share exchanged. (App. 4a.) Immediately preceding the merger, Auto-Lite had 1,159,265 common shares outstanding and Mergenthaler had 2,698,822 common shares outstanding. Both stocks were actively traded on the New York Stock Exchange. (PX 1, pp. 16, 47, 59.)

preferred stock in July 1963 was $58.39. (App. 18a.) Thus, the merger resulted in a gain in market value of $6.14 per share for the Auto-Lite shareholders. The Mergenthaler shareholders realized a gain of only 37½¢ per share as a result of the merger.[6]

Dividends. In 1961 and 1962, the Auto-Lite shareholders had received a $2.40 annual dividend. Under the merger terms, the Eltra preferred stock afforded the Auto-Lite shareholders a $2.63 dividend. (App. 5a.) The Mergenthaler shareholders continued to receive a $1.00 annual dividend which was subordinated to the preferred dividend. (App. 5a.)

Earnings. In the merger exchange, the Auto-Lite shareholders were credited with $4.56 in annualized earnings, which exceeded Auto-Lite's actual earnings for either fiscal or calendar 1963.[7] This was also more than Auto-Lite earned in any of the five years preceding the merger. (PX 1, p. 14.)

In summary, the merger exchange offered the Auto-Lite shareholders a security in a merged company with a diversified base of business from which to generate profits. The merger provided the Auto-Lite shareholders with an increase in market value, more stable earnings, a higher dividend with greater security, and a claim ahead of the Mergenthaler shareholders on all of the assets of both companies in the event the merger proved unsuccessful.

---

[6] The average weekly market price of Mergenthaler shares in the first quarter of 1963 was $24.875. (App. 17a-18a.) The average price of Eltra common in July 1963 was $25.25. (App. 18a.)

[7] Earnings for the six-month period ended March 31, 1963 were $2.28 (PX 1, p. 14) or $4.56 annualized. For the fiscal year ended September 30, 1963, Auto-Lite earned $3.93. (Tr. 5153-55.) For calendar 1963, Auto-Lite earned $4.36. (Tr. 5168.)

The Trial.

Following remand from this Court, a three-month trial was conducted on the issue of relief, generating a record of 8,200 pages. Petitioner's case consisted solely of the testimony of two expert witnesses, Dr. George H. Sorter and Dr. Erwin E. Nemmers, together with documentary evidence. (App. 27a.)

In support of his damage theory, Dr. Sorter purported to analyze the post-merger operations of the former Auto-Lite and Mergenthaler divisions for a ten-year period following the merger. The District Court found that Dr. Sorter's testimony was "unrealistic," that it was based upon "several substantially erroneous assumptions," and that it could not "reliably serve as a basis for computing injury." (App. 56a.)

Dr. Nemmers testified that, in his opinion, the merger ratio was unfair because the Eltra preferred stock received in the merger exchange had a value of only $49.24. (Tr. 6147-48.) The District Court found that the value of the Eltra preferred stock at the time of the merger was $58. (App. 69a-70a.)

Respondents introduced evidence demonstrating that the merger was fair and beneficial to the Auto-Lite shareholders and that petitioner had suffered no damages. Respondents called as expert witnesses Professor James H. Lorie, Professor Richard F. Vancil, Robert Emmett of Standard Research Consultants, George V. Carracio of Arthur Young & Co., and Michael J. Quinn of Price Waterhouse & Co. In addition, several officers and employees of Eltra testified as to the background of the companies and the formulation of the merger terms. (App. 27a.)

The Decision Of The District Court.

The District Court issued its opinion in April 1975. The Court found that there had been substantial commingling of the assets and operations of Auto-Lite and Mergenthaler following the merger. (App. 54a-56a.) The Court also found the evidence insufficient to allow application of the "earnings or earnings potential" test. (App. 56a-57a.) Accordingly, the District Court looked to the fairness of the merger terms to determine whether damages should be awarded. (App. 57a.)

After arriving at what it concluded to be a fair merger ratio, the District Court computed damages based on the difference between that ratio and what the Court found the Auto-Lite shareholders had received in the merger exchange. (App. 70a.) The District Court awarded damages of $1,233,918 plus prejudgment interest. (App. 70a-71a, 79a.)[8] The District Court also held that petitioner's attorneys' fees and expenses for all proceedings in the case should be paid out of the damage award. (App. 71a-73a.)

The Unanimous Decision Of The Court Of Appeals.

The Court of Appeals affirmed the District Court's finding of commingling. (App. 8a.) In accord with this Court's mandate, the Court of Appeals ruled that the District Court properly found that fairness of the merger terms should be the applicable test for damages in this case. (App. 4a, 9a.)

---

[8] The Court of Appeals found that the District Court's calculation of damages was "mathematically unsound" and involved an "arithmetic error." (App. 10a, n.6.) Petitioner conceded in the Court of Appeals that the District Court had made a mathematical error and that the correct damage computation under the District Court's formula should have been approximately $410,000 rather than $1,233,918. (Pet. Ct. of App. Br. 91 n.1.)

The Court of Appeals then reviewed the relevant evidence and determined that the merger terms were fair. The Court of Appeals found that rather than suffering damages, the Auto-Lite minority shareholders substantially benefitted from the merger. Accordingly, the Court held that petitioner should recover no damages. The Court stated (App. 19a):

> "A numerical example may help to show the justice of this result. In early 1963, an Auto-Lite shareholder with one hundred shares and a Mergenthaler shareholder with 210 shares each owned stock worth approximately $5225. After the merger, the former Auto-Lite shareholder had 188 shares of Eltra preferred worth approximately $5839 while the former Mergenthaler shareholder had 210 shares of Eltra common worth approximately $5302. Both individuals benefitted from the merger, but the former Auto-Lite minority shareholder benefitted more."

The Court of Appeals held that petitioner was not entitled to an award of fees and expenses for his unsuccessful attempt to prove damages. It ruled that petitioner did not come within any exception to the American rule against fee shifting. The Court found that plaintiffs had conferred "no benefit upon the class they represent beyond the 'corporate therapeutics' produced by their showing that the proxy statute was violated . . . ." (App. 21a.) Accordingly, the Court held that fees and expenses should be awarded to petitioner only for establishing liability and remanded the case for a hearing to determine the amount of that award. (App. 19a-21a.)

REASONS FOR DENYING THE WRIT

I.
THE MANDATE OF THIS COURT HAS BEEN FULFILLED.

This Court ruled in *Mills* that if the assets and operations of the merged companies were commingled, the "earnings or earnings potential" test would not be applicable in this case. Rather, the Court stated that where commingling occurred, the need for relief could be determined by evaluating the fairness of the merger terms. 396 U.S. at 388-89. The Court further ruled that in the absence of damages, petitioner nevertheless would be entitled to an award of attorneys' fees for establishing liability. 396 U.S. at 396-97. The decision of the Court of Appeals carefully followed the mandate of this Court.

A. The Lower Courts' Rejection Of Petitioner's Post-Merger Damage Theory Requires No Further Review.

(Answer to Petition 7-8; 21-28.)

(1) Commingling Precluded The Application of Petitioner's Post-Merger Damage Theory.

The District Court found that the assets and operations of Auto-Lite and Mergenthaler were commingled during the ten-year period following the merger. The District Court also concluded that all the shareholders benefitted from the fusion of the assets and managerial talents of the merged companies. (App. 54a-56a.)[9]

[9] Petitioner charges that the District Court did not find that commingling had occurred. (Pet. 8, 26-27.) The explicit findings of the District Court on this subject are found at App. 54a-56a. At trial, respondents presented overwhelming and uncontroverted evidence that commingling had in fact occurred. (Tr. 2472-73, 2477, 2491-93, 2501-02, 2505-06, 3594-95, 3632-34, 3640, 3642-43, 3647-50, 3684, 3712-14, 4543-45, 4722, 4811-35; PX 3, 4, 12, 83; DX 39B, 46-46A, 60-64.)

The Court of Appeals specifically affirmed the District Court's finding of commingling as "supported by substantial evidence." (App. 8a.) The Court of Appeals further held that the District Court "did not abuse its discretion in refusing to award damages based on postmerger data." (App. 9a.) In light of these findings, both the District Court and the Court of Appeals correctly determined, in accord with this Court's decision in *Mills*, that damages in this case could not be awarded under the earnings and earnings potential test.

(2) Petitioner's Post-Merger Damage Theory Was Not Sustained By The Evidence.

In addition to the finding of commingling, both courts below found that petitioner failed to submit reliable evidence in support of his post-merger damage theory. Disregarding these findings, petitioner urges in this Court that Eltra's records demonstrated damages totaling $7,146,856 based upon post-merger operations. (Pet. 25.)[10]

Respondents' expert, George V. Carracio of Arthur Young & Co., testified that Eltra's records could not be utilized to ascertain what Auto-Lite's operating results would have been had no merger occurred. (Tr. 4504-05; 4529-37.) Professor Vancil of the Harvard Business School testified to the same effect. (Tr. 4808.) The District Court found that the testimony of petitioner's expert, Dr. Sorter, was "unrealistic" and based upon "several sub-

[10] In the trial court, petitioner claimed post-merger damages of $69,245,530. (Pet. Post-Trial Br. 92-93.) In the Court of Appeals, petitioner changed this figure to $29,376,835. (Pet. Ct. of App. Br. 62, 111, 121, 127.) In his petition for rehearing, petitioner adopted the $7,146,856 figure urged here. (Pet. for Rehrg. 26.) That petition alternatively claimed damages of $989,567 as "defendants' profits." (Pet. for Rehrg. 26 n.1.)

stantially erroneous assumptions." (App. 56a; 56a, n.3.)[11] After reviewing the evidence, the District Court found that the records relied upon by petitioner could not sustain a damage award. (App. 54a-55a.) The District Court accordingly ruled (App. 56a-57a):

> "I find in this case not enough evidence of sufficient reliability to utilize the earnings and earnings potential concept as a basis for measuring damages. This does not mean that in the next case the evidence could not be substantial and convincing."

The Court of Appeals affirmed the District Court's findings that petitioner's post-merger damage theory was not supported by the evidence. (App. 6a-9a.)

Thus, the lower courts rejected petitioner's post-merger damage theory both because of commingling and because of petitioner's failure of proof. When two lower courts concur on findings of fact, this Court will not provide further review. *See Berenyi* v. *Immigration Director,* 385 U.S. 630, 635-36 (1967); *Graver Manufacturing Co.* v. *Linde Co.,* 336 U.S. 271, 275 (1949).

(3) Petitioner's Post-Merger Damage Theory Failed As A Matter Of Law.

Dr. Sorter purported to analyze the post-merger operations of the former Auto-Lite and Mergenthaler divisions for a ten-year period following the merger. As the District Court recognized, it was Dr. Sorter's theory that any intracorporate transfers of assets from the Auto-Lite divi-

[11] In addition, Dr. Sorter's testimony concerning Eltra's records was riddled with errors. On appeal, petitioner conceded that Dr. Sorter made errors amounting to $13.5 million. (Pet. Ct. of App. Br. 56-57.) Petitioner did not address Dr. Sorter's other errors totaling at least another $83.9 million. (Resp. Ct. of App. Br. App. 76-78.) Dr. Sorter's analysis also ignored $200 million of adjusting journal entries. (Tr. 115; DX 2-11.)

sions to Eltra headquarters should be treated as "dividends" which should have been paid to the former Auto-Lite shareholders. (App. 53a-56a.) Petitioner has variously referred to his post-merger damage theory as involving "transfers," "withdrawals," "distributions," and "dividends." Currently, petitioner characterizes his theory as a calculation of "defendants' profits." (Pet. 2, 21-28.)[12]

Petitioner is incorrect in treating all post-merger transfers of assets as "defendants' profits." Nothing was paid out of the corporation by reason of these transfers, which were made for the purpose of efficient corporate management. Moreover, the Auto-Lite minority received Eltra stock and participated in all the benefits flowing from the merger. Thus, this case does not involve a "squeeze-out" (Pet. 9), where the minority is excluded from ownership and future profits generated by the corporation's assets. See *Santa Fe Industries, Inc.* v. *Green,* ..... U.S. ....., 45 U.S.L.W. 4317 (1977). Under the facts of this case, the District Court properly rejected petitioner's post-merger damage theory. (App. 53a-57a.)

After reviewing petitioner's contention, the Court of Appeals affirmed the findings of the District Court and ruled that respondents had not profited at the expense of the Auto-Lite minority (App. 6a):

> "After the merger the former Auto-Lite shareholders had become Eltra shareholders and had no more interest in the Auto-Lite divisions than any other Eltra shareholder. Therefore, they could not be injured

[12] While petitioner sometimes argues in his petition in terms of "earnings" (Pet. 25-26), he did not try the case on this theory. See App. 7a. Indeed, petitioner stated to the District Court, "Whether the income of Eltra would have been different had there been no merger is not material to Sorter's testimony or theory because it would not affect the distribution of assets that occurred." (Pet. Post-Trial Br. 88 n.44.)

> by intracorporate transfers of assets designed to strengthen the corporation as a whole. The interests of the former Auto-Lite shareholders and former Mergenthaler shareholders coincided after the merger, and the Eltra management could not possibly take actions that benefitted 'its' shareholders at the expense of the Auto-Lite shareholders."

The Court of Appeals also correctly determined that the authorities upon which petitioner relies (Pet. 22-25) could not support an award of damages under the facts of this case. (App. 6a-7a.) In *Gerstle* v. *Gamble-Skogmo, Inc.*, 478 F.2d 1281, 1304 (2d Cir. 1973), plaintiffs, like petitioner here, argued that defendants had wrongfully "profited" from "the appreciation of properties obtained unlawfully through the merger." Contrary to petitioner's assertion (Pet. 24-25), the Second Circuit rejected this damage theory. 478 F.2d at 1306.

Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972), also relied upon by petitioner (Pet. 22-25), involved fraud under Section 10(b). The defendants in *Ute* engaged in a face-to-face scheme to defraud the Ute Indians by inducing them to sell their stock without disclosing to them its fair market value. The defendants promptly resold the stock at a substantial profit, and this Court held that these profits could be recovered as damages. 406 U.S. at 155.[13]

Ute thus arose in a factual setting completely dissimilar from this case. Here, instead of selling their stock for

[13] In *Gerstle*, Judge Friendly distinguished *Ute* and *Janigan* v. *Taylor*, 344 F.2d 781 (1st Cir.), *cert. denied*, 382 U.S. 879 (1965), on the ground that those cases involved defendants who "had purchased stock at a low price by misrepresenting its value and had resold it prior to suit at a large profit." 478 F.2d at 1304.

cash, the Auto-Lite minority exchanged their shares for stock in the merged company. By November 1968, one former Auto-Lite share having a pre-merger value of $52.25 had risen in the market to $200. (DX 108B.) A minority shareholder who, like the former plaintiff Susman, owned 500 shares of Auto-Lite stock worth $26,125 at the time of the merger, saw his investment appreciate within five years after the merger to $100,000.[14] It is apparent that the Auto-Lite minority was not damaged and in fact benefitted from the merger.

The courts below rejected petitioner's post-merger damage theory as lacking in both factual and legal support. Accordingly, under this Court's mandate, the courts below properly held that any potential damage award in this case should be measured by the fairness of the merger terms.

B. The Factual Determination That The Merger Terms Were Fair Raises No Question Worthy Of Consideration By This Court.

(Answer to Petition 6-7; 8-21.)

(1) The Weight Of The Evidence Demonstrated The Fairness Of The Merger Terms.

The evidence submitted at trial provided clear confirmation of the fairness of the merger terms.

Prior to the merger, Standard Research Consultants, a division of Standard & Poor's Corporation, independently reviewed the proposed merger terms on behalf of the Auto-

[14] In addition to the appreciation in market value, the former Auto-Lite shareholders received an increase in dividends from $2.40 per share prior to the merger to $5.90 by the time of trial. (Tr. 2523.)

Lite minority shareholders. Based upon statistical and financial analysis of market values, earnings, dividends, book values, and other factors, Standard Research concluded that the merger was fair and beneficial to the Auto-Lite minority. (DX 45-45D.)

Professor Lorie, a leading authority in securities analysis, testified that the merger terms were fair. (Tr. 5409-12.) He confirmed his opinion by utilizing the Bank of New York formula, a recognized statistical method relied upon by financial institutions to judge the advisability of corporate investments. (Tr. 5282-93.) Mr. Emmett of Standard Research also testified that the merger terms were fair. (Tr. 4283-86.)

Only petitioner's expert, Dr. Nemmers, testified that the merger terms were unfair. His opinion was that the Eltra preferred stock offered in the merger was worth no more than $49.24. (App. 69a.) However, immediately following the merger, the market placed a value of $58.39 on the Eltra preferred shares. (App. 70a-71a.) The District Court correctly found that Dr. Nemmers' testimony was not borne out in the market place. (App. 69a-70a.)[15]

(2) The Court Of Appeals Properly Determined That The Merger Terms Were Fair.

The Court of Appeals found that the Eltra preferred stock was "clearly worth more than Eltra common because it paid a higher dividend and represented a more secure investment if the new corporation encountered financial

[15] In the course of his analysis, Dr. Nemmers made numerous errors, including 11 mistakes in a one-page exhibit and a $16 million miscalculation in another exhibit. (PX 38, 116; DX 33; Tr. 6047, 6137-38.)

difficulties." (App. 5a.) The Court further ruled that Auto-Lite's uncertain future was a factor to be considered in arriving at the merger terms. (App. 16a.)

In evaluating the fairness of the merger, the Court of Appeals found that the stock of Auto-Lite and Mergenthaler was actively traded on the New York Stock Exchange in a free and reliable market.[16] The Court accordingly determined that market price should be the primary gauge of value under the particular facts of this case (App. 16a):

> "Although criteria such as earnings and book value are an indication of actual worth, they are only secondary indicia. In a market economy, market value will always be the primary gauge of an enterprise's worth. In this case thousands of shares of Auto-Lite and Mergenthaler were traded on the New York Stock Exchange during the first part of 1963 by outside investors who had access to the full gamut of financial information about both corporations, including earnings and book value."

In attacking this ruling as unprecedented (Pet. 7), petitioner ignores his own evidence submitted at trial. Dr. Nemmers, petitioner's sole witness on fairness, testified that where the market is free and reliable, primary emphasis should be placed on market values. (Tr. 1134, 1529.) Petitioner adopted the same position in his trial and appellate court briefs. (Pet. Post-Trial Br. 76, 121; Pet. Ct. of

[16] Although petitioner attacks this ruling on the reliability of the market, the District Court made a similar finding (App. 46a-47a):

> "[T]he evidence shows only minor trading by American in Mergenthaler stock after the early part of 1962, and none by Mergenthaler in Auto-Lite stock after the early part of 1962. There is no competent evidence of any major attempt by or opportunity for either American or Mergenthaler to influence the prices at or near the time of the merger . . . ."

App. Br. 42.) Petitioner's position on market value in this Court is thus a reversal of the argument he presented to both courts below.[17]

In ruling that market price in this case was "an accurate gauge of actual value" (App. 16a), the Court of Appeals followed well-established precedent. As Judge Learned Hand stated in *Borg* v. *International Silver Co.*, 11 F.2d 147, 152 (2d Cir. 1925):

> "When all is said, value is nothing more than what people will pay for the shares, given as wide an opportunity for bidders to come in as is reasonably possible."[18]

---

[17] The decisions on which petitioner now relies (Pet. 9-12) do not support his criticism of the use of market value in this case. There was no market whatever for the stock in *Pepper* v. *Litton*, 308 U.S. 295 (1939). In *E. I. duPont de Nemours & Co.* v. *Collins*, ... U.S. ....., 45 U.S.L.W. 4668 (1977), the Court affirmed the valuation of an investment company's stock based on the market value of the duPont stock which it held. In *Schwabacher* v. *United States*, 334 U.S. 182, 201 (1948), the Court held that the ICC should consider dividend arrearage claims in a railroad merger only if they "affect intrinsic or market values." In *In re Talley Industries, Inc.*, SEC Investment Company Act Release No. 5953, [1969-70 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶77,774 at 83,792 (1970), the SEC rejected market value as a determinant of fairness in a proposed merger because recent "sizeable acquisitions of new companies" by the acquiring corporation had made its market price unreliable. In *Dasho* v. *Susquehanna Corp.*, 461 F.2d 11 (7th Cir.), *cert. denied*, 408 U.S. 925 (1972), the Court of Appeals reversed a trial judge's finding that merger terms were fair, because the defendant had been deprived of a jury trial and because market value evidence might have allowed a jury to reach a different decision.

[18] *See also Levin* v. *Mississippi River Corp.*, 59 F.R.D. 353, 370 (S.D.N.Y. 1973) ("Theory must yield to the reality of the market place, 'the true appraiser.'"); *David J. Greene & Co.* v. *Schenley*

(footnote continued)

In testing the fairness of the merger terms, the Court of Appeals considered the market values of Auto-Lite and Mergenthaler stock in 1963, prior to the formulation of the merger terms, and determined that one share of Auto-Lite was worth 2.1 shares of Mergenthaler. (App. 15a.) The Court then found that, in the merger exchange, the Auto-Lite shareholders received stock worth "2.31 times as much on the market as the stock that the Mergenthaler shareholders received." (App. 5a.) Thus, the Auto-Lite minority shareholders received "more Eltra stock than they were entitled to in the judgment of the market." (App. 17a.)

In an effort to overcome the fact that the Auto-Lite shareholders were clearly benefitted by the merger exchange, petitioner urges that respondents "timed" the merger to the disadvantage of the minority and withheld information from the market. (Pet. 13-18.) These same arguments were presented to and rejected by the District Court. After reviewing the evidence, the District Court stated (App. 74a-75a):

> "I am particularly impressed by evidence presented by the defendants on the issue of good faith during the formation and adoption of the merger terms. . . ."

Petitioner also urges that the Court of Appeals examined market values over too short a span of time. (Pet.

(footnote continued)

Industries, Inc., 281 A.2d 30, 34 (Del. Ch. 1971) ("[M]arket price, when it can be established by free trading in an open forum, is, in my opinion, the most significant element to be taken into consideration in reaching a judgment on the overall fairness of a corporate merger."); *Gallois* v. *West End Chemical Co.*, 185 Cal. App. 2d 765, 774, 8 Cal. Rptr. 596, 602 (1960) ("[R]ealistically, under our economic system, the value of any item of property on any given date, in monetary terms, is what it can be sold for in a free and fair market.")

18-19.) To the contrary, the Court of Appeals noted (App. 15a):

> "Our confidence that this figure [the 2.1 ratio] accurately reflects the relative worth of the two corporations is bolstered by the fact that the ratio for 1962 was also 2.1 and was 2.0 for 1961. The similarity of these numbers is evidence that the ratio immediately preceding the merger was not the result of a short term anomaly caused either by the merger itself or by other factors."

Finally, petitioner would have this Court overlook the fact that the Court of Appeals employed the most liberal formula available to ensure that the Auto-Lite shareholders were treated fairly. The Court of Appeals did not rest upon its finding that the merger provided more than fair value to the Auto-Lite minority shareholders based on pre-merger market values. Rather, the Court adopted an additional test formulated by Professors Brudney and Chirelstein to protect minority shareholders in parent-subsidiary mergers.[19] The Court stated (App. 17a):

> "[F]airness requires that minority shareholders be compensated not only for the market value of their shares in the old corporation but also for the share of the synergism generated by the merger that is proportionate to the interest that those shares represented in the combined premerger value of the two old corporations."

[19] Brudney & Chirelstein, *Fair Shares in Corporate Mergers and Takeovers*, 88 Harv. L. Rev. 297 (1974). In this article, the authors conclude that the tests traditionally employed to measure the value of minority stock in parent-subsidiary mergers are inadequate. *Id.* at 299-307. The authors note that mergers may result in a combined entity whose market value is greater than the sum of the pre-merger market values of the two corporations taken separately. *Id.* at 308. Traditional tests permit a parent merging with a subsidiary to appropriate for itself all of this increase in market value or "synergism." The new test formulated by the authors, which is based on the principle that management must act as a trustee for minority shareholders, requires that the increase be shared proportionately between the shareholders of the parent and subsidiary. *Id.* at 318-25.

Applying the Brudney and Chirelstein formula, the Court of Appeals found that, while the Auto-Lite shareholders received stock with a market value of $31,095,594, they were entitled only to stock worth $29,080,338. Thus they were paid "$2,015,256 more than fairness required." (App. 19a.)

In rendering its decision, the Court of Appeals applied the mandate of this Court to the particular facts of this case. There is no reason for this Court to review the factual findings demonstrating the fairness of the merger. *See, e.g., General Talking Pictures Corp.* v. *Western Electric Corp.*, 304 U.S. 175, 178 (1938) ("Granting of the writ would not be warranted merely to review the evidence or inferences drawn from it.")

C. Denial Of Additional Attorneys' Fees By The Court Of Appeals Does Not Merit Review By This Court.

(Answer to Petition 8; 28-30.)

The Court of Appeals has remanded this case to the District Court to award attorneys' fees to petitioner for having established liability. However, because of its finding that petitioner was not damaged by the merger, the Court of Appeals held that, under the circumstances of this case, petitioner is not entitled to an additional fee award.

Contrary to petitioner's assertion (Pet. 28-29), the denial of additional fees in no way conflicts with the mandate of this Court. This Court stated that petitioner might receive fees and expenses in connection with the damage proceedings only if the record established "the need for

a further award." 396 U.S. at 390 n.13. This Court indicated that the request for a further award must be judged in part by "[w]hether petitioners are successful in showing a need for significant relief." 396 U.S. at 396. Because petitioner was not damaged by the merger and showed no need for relief, the Court of Appeals correctly held that petitioner is not entitled to any additional fee award in this case.

In making its determination, the Court of Appeals properly considered and applied the decision in *Alyeska Pipeline Service Co.* v. *Wilderness Society,* 421 U.S. 240 (1975). *Alyeska* rejected an expansive reading of *Mills,* which some lower courts had interpreted as precedent for awarding fees under a "private attorney general" theory. As this Court stated in *Alyeska,* "[T]he circumstances under which attorneys' fees are to be awarded and the range of discretion of the courts in making those awards are matters for Congress to determine." 421 U.S. at 262. Absent statutory authority, the only exceptions to the American rule that a litigant must pay his own fees and expenses are those situations where a losing party acts in bad faith or where a litigant confers a common benefit on the class he represents. 421 U.S. at 257-259.

Petitioner does not contend that there is any statutory basis for a fee award in this case. Nor does petitioner take issue with the Court of Appeals' ruling (App. 21a) that the bad faith exception to the American rule is inapposite here.[20] Instead, by analogizing his role in

[20] Although this case has been pending fourteen years, the District Court found that "[v]ery little, if any, delay in these proceedings was caused by the defendants." (App. 77a.) The District Court also found that "the defendants have not acted in bad faith, vexatiously, wantonly or for oppressive reasons . . . . Nor have defendants acted frivolously." (App. 72a.)

this litigation to that of a "guardian ad litem" or "receiver," petitioner urges that he conferred some common benefit on the Auto-Lite minority shareholders. Petitioner argues that because this case is a derivative action, he is entitled to fees and expenses, even in the absence of a common fund, for having acted in the name of the corporation. (Pet. 30.)

Petitioner's claim for additional fees lacks merit. As the Court of Appeals recognized, the merger was more than fair by $2 million and petitioner is entitled to no damages. (App. 19a.) No matter how he attempts to characterize his role in this litigation, petitioner cannot escape the fact that he did not confer a benefit upon the Auto-Lite minority shareholders in the damage proceeding. Having failed to confer any benefit, petitioner falls within no exception to the American rule and must pay his own fees and expenses for his unsuccessful attempt to obtain damages.

The result reached by the Court of Appeals is further supported by this Court's analysis in *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 185, 210-11 n.30 (1976). There the Court noted that the power of the courts to award attorneys' fees in securities cases "is sharply circumscribed." That admonition forecloses adoption of the exception to the American rule proposed by petitioner here. However, pursuant to the direction of this Court in *Mills,* petitioner on remand from the Court of Appeals will be entitled to reasonable fees for establishing liability.

II.

THIS CASE IS INAPPROPRIATE FOR THIS COURT'S REVIEW BECAUSE THE LEGAL STANDARD OF MATERIALITY IN TSC V. NORTHWAY WAS NEVER APPLIED BELOW.

After the Court of Appeals heard oral argument in this case, but prior to the issuance of its decision, this Court decided *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438 (1976). Because the Court of Appeals determined that petitioner was not damaged, there was no need for it to reach the issue of materiality under the standard enunciated in *TSC*.[21]

Under *TSC*, an alleged defect in a proxy statement is material only if it "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." 426 U.S. at 449. The sole proxy violation found by the courts in the entire fourteen-year history of this case would not have satisfied this standard. On petitioner's motion for summary judgment, the Auto-Lite proxy statement was held to be defective simply because of the use of bold-face type in setting forth the recommendation of the Auto-Lite board, without placing similar emphasis on the control relationship between Mergenthaler and Auto-Lite. 403 F.2d at 433-34. However, the control relationship was clearly and repeatedly disclosed.[22] The failure to place the control relationship in bold-face type could not have been viewed by a reasonable Auto-Lite shareholder as having "significantly

[21] This Court in *Mills* specifically declined to consider the materiality of the omission. 396 U.S. at 381 n.4. See also *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. at 447.

[22] Immediately preceding the board's recommendation for shareholder approval of the merger, the shareholders were informed that Mergenthaler owned 54% of Auto-Lite's stock and intended to vote in favor of the merger. The proxy statement also disclosed that Mergenthaler held a "majority" and "controlling" interest in Auto-Lite, that no other shareholder owned more than 10% of the Auto-

(footnote continued)

altered the 'total mix' of information made available," in view of the disclosures regarding control which appeared throughout the Auto-Lite proxy statement.

The SEC has stated that the proxy statement here made fuller disclosure than the one in *TSC*:

> "[T]here was greater disclosure in *Mills* than [in *TSC*] concerning the overlapping management of the two companies. And, significantly, the proxy statement in *Mills* expressly disclosed the fact of *majority* control." (SEC amicus brief filed with Seventh Circuit in *TSC Industries, Inc.* v. *Northway, Inc.*, at p. 11.)

The deficiency in the proxy statement found by the courts below would not be a material defect under the standard enunciated in *TSC*.[23] However, *TSC* has never been applied to the case at bar. All pending and future cases brought under Section 14(a) will be adjudicated under the *TSC* standard. Accordingly, the present case could not serve to clarify existing law and is factually unsuitable for establishing precedent. In addition, certiorari should be denied since *TSC* provides an alternative ground for affirming the judgment below. *See United States* v. *American Railway Express Co.*, 265 U.S. 425, 435-36 (1924).

(footnote continued)

Lite stock, that the directors of Auto-Lite and Mergenthaler were interlocking, and that Auto-Lite had been treated as a "consolidated subsidiary" of Mergenthaler. (PX 1, pp. 2, 6, 7, 21-23, 33, 35, 37, 44, 47, 49, 50, 52, 54.) See also 403 F.2d at 433.

[23] Perhaps recognizing that the violation found in this case would not be held material under *TSC*, petitioner argues at length regarding additional alleged proxy violations. (Pet. 4-5 n.1.) The same arguments were presented to both courts below without success. None of these charges has any basis in the record. For example, petitioner alleges that it was improper not to include a "stub year" comparison in the proxy statement. In fact, the Chief Accountant of the SEC Division of Corporation Finance, in a pre-issue review of the proxy statement, concluded that such a comparison should be eliminated as misleading to the shareholders. (Tr. 5785-94.)

III.

THE REFUSAL TO AWARD DAMAGES IN THE ABSENCE OF MONETARY INJURY IS IN ACCORD WITH ESTABLISHED LAW.

Although the Auto-Lite minority benefitted greatly from the merger, petitioner nevertheless demands damages. Simply stated, petitioner argues that any finding of liability in a Section 14(a) case requires an award of damages, even in the absence of monetary injury. (*See, e.g.*, Pet. 6, 11, 12, 18.)

In *Mills,* this Court stated that petitioner would not be entitled to damages unless he could prove that financial injury resulted from the merger. "[D]amages should be recoverable only to the extent that they can be shown." 396 U.S. at 389. Recognizing that the defect here did not relate to the merger terms, the Court noted that this case might never produce a monetary recovery. 396 U.S. at 392, 396.

This Court recently interpreted its language in *Mills,* stating:

> "*Mills* could not be plainer in holding that the questions of liability and relief are separate in private actions under the securities laws, and that the latter is to be determined according to traditional principles." *Rondeau* v. *Mosinee Paper Corp.*, 422 U.S. 49, 64 (1975).

Applying this reasoning, this Court held that the plaintiff in *Rondeau* was not entitled to relief despite the fact that the defendant had clearly violated Section 13(d) of the Williams Act. The Court noted that the violation in *Rondeau* was only "technical" and directed that the case be

dismissed without relief to the plaintiff. 422 U.S. at 56, 64-65. The Court held that a plaintiff must show harm other than the legal injury caused by the violation itself. The Court also expressly rejected the argument, suggested by petitioner here, that a plaintiff is relieved from proving harm because litigation in this area vindicates the public interest in assuring full compliance with the securities laws. 422 U.S. at 62-63.

Petitioner's claim in this case is disingenuous in light of the fact that immediately upon receipt of the proxy statement, some three weeks before the shareholders' meeting, petitioner retained counsel who chose to wait until the day before the meeting to file his complaint. Petitioner did not notify management of the claimed defect, seek redress from the SEC, or request a judicial postponement of the meeting. Counsel for petitioner informed the District Court that he deliberately chose not to seek preliminary relief. (Tr. 92-93, hearing, April 15, 1966.) Respondents should not be required to pay damages merely because petitioner pursued the tactic of not seeking an appropriate remedy that would have avoided fourteen years of litigation.

This Court has indicated its disapproval of speculative theories of recovery which are unrelated to actual losses. *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 734-35 (1975). *See also Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.,* 429 U.S. 477, 490 (1977). The rationale behind petitioner's argument that he is entitled to damages in the absence of monetary injury was rejected in *Bangor Punta Operations, Inc.* v. *Bangor & Aroostook Railroad,* 417 U.S. 703 (1974). The Court noted that acceptance of such an argument would mean:

> "No injury . . . would have to be alleged. The only prerequisite would be that the plaintiff agree to accept the recovery, lest the supposed wrongdoer be allowed to escape a reckoning. Suffice it to say that we have been referred to no authority which would support so novel a result, and we decline to adopt it." 417 U.S. at 717.

The Court of Appeals properly declined to award damages and provided the only relief appropriate under the mandate of this Court and the facts of this case—a remand for the determination of reasonable fees and expenses to be allowed petitioner for establishing liability.

CONCLUSION

For the reasons set forth above, it is respectfully submitted that the petition should be denied.

Respectfully submitted,

JEROLD S. SOLOVY
JOAN M. HALL
Attorneys for Respondents.
One IBM Plaza
Chicago, Illinois 60611

JENNER & BLOCK

MICHAEL J. ROVELL
ROBERT L. GRAHAM
JAYNE W. BARNARD
EUGENE R. WEDOFF
Of Counsel

Dated: September 30, 1977